MEMO

DATE: January 5, 2005

TO: Community, Economic and Human Development Committee

FROM: Don Rhodes

SUBJECT: President's Advisory Panel on Tax Reform: Mortgage Interest Deduction

SUMMARY:
On November 1, 2005 the President's Advisory Panel on Tax Reform issued their final report which included numerous recommendation relating to our national Tax Code. Some of their recommendations call for reforms to the mortgage interest deductibility. The following table briefly describes the recommended changes:

	Current Law	Recommendation
Mortgage Interest Deduction verses Tax Credit	Homeowners are allowed to deduct interest paid on up to $1 million of mortgage debt secured on a first or second home and an additional amount on home equity loans of up to $100,000.	The panel recommends • replacing the deduction for mortgage interest with a Home Credit available to all taxpayers equal to 15% of interest paid on principle residence • establish an amount of mortgage interest eligible for the Home Credit based on average regional housing costs • eliminate the deduction for interest on mortgages for second home • eliminate the deduction for interest on home equity loans. *changes would be phased in over 5 years
Capital Gains	Up to $500,000 of capital gains on a home that a taxpayer has owned and used as a principle residence for two or more years may be excluded.	Maintain the exemption of capital gains, but extend the minimum time period to 3 years.

BACKGROUND:
At this point, it is unclear how severely these changes will affect homeowners in southern California. However, many homeowners rely on mortgage interest deductions to offset a portion of their cost of housing. In high cost housing regions, such as Southern California, these changes would affect homeowners most.

The President is reviewing the Panel's recommendations, and we may see legislation containing these proposed changes during the Congressional session.

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